DEBT GUIDELINE STEERING COMMITTEE

REPORT

December 1985

INTRODUCTION

In October 1983, the Minister of Municipal Affairs' Advisory Committee on the Debenture Approval Process recommended, among other things, the following:

> "That an independent consultant, well experienced in the municipal and financial fields, be retained to consult with municipalities of different sizes, the Local Authorities Board and the Alberta Municipal Financing Corporation to establish a working formula or model regarding borrowing/debt guidelines and/or limitations that can be easily administered and readily understood by all concerned."

On November 5, 1984, the Minister of Municipal Affairs announced the formation of a Debt Guideline Steering Committee consisting of the following members:

C. I. Shelley, Chairman, representing the Local Authorities Board

V. D. Van Orman, Mayor of the Town of Taber, representing the Alberta Urban Municipalities Association

J. S. Smith, Reeve of the County of Barrhead, representing the Association of Municipal Districts and Counties

H. H. Strohbach, General Manager, Alberta Municipal Financing Corporation

J. M. Fleming, Director of Municipal Services Branch, Department of Municipal Affairs

The purposes of the Committee as set forth by the Minister were:

1. To draft terms of reference for a consultant study of borrowing or debt guidelines and/or limits and issue a request for proposals to qualified consultants;

2. To review proposals received and recommend a consultant for appointment;

3. To act as a steering committee and liaison group with the consultant for the duration of his work;

4. To advise the Minister of Municipal Affairs on the report of the consultant.

The Committee was supposed to issue its request for proposals prior to January 31, 1985, and forward its report to the Minister by the end of 1985.

The Committee met on nine occasions. The first meeting was held on December 11, 1984, and after fulfilling the above noted objective No. 1, proposals for the study were received on February 27, 1985, from five consulting firms.

On March 18, 1985, the Committee recommended to the Minister of Municipal Affairs:

1. To approve the appointment of the firm of Deloitte, Haskins & Sells Associates to carry out the requested study;

2. That said Consultants be paid the amount of $69,500 as full payment for the work performed;

3. That in accordance with Section 12 of the Local Authorities Board Act, an Order in Council be adopted concerning said appointment;

4. That a contract be entered into between the above named Consultants and the Local Authorities Board;

5. That the amount of $69,500 be transferred in the 1985/86 budget of the Local Authorities Board from the surplus category of Manpower Costs (001) to Supplies and Service Costs (002), Item 430 (Consulting Services).

Upon the recommendation of the Minister of Municipal Affairs, Order in Council 199/85 was passed on March 27, 1985, approving the appointment of Deloitte, Haskins & Sells Associates to carry out a study to evaluate the debt guidelines and/or limits for municipalities at a remuneration of $69,500.

The Agreement between the Local Authorities Board and the Consultants was signed on April 3, 1985.

Five meetings were held with the Consultants; the first one April 10, 1985, and the last one on October 1, 1985.

During the first meeting the Consultants outlined the study objectives and the proposed approach. After the review of the legislation, literature and database, statements of selected municipalities were analysed, interviews held with the Local Authorities Board, the Alberta Municipal Financing Corporation, the Alberta Urban Municipalities Association, the Alberta Association of Municipal Districts and Counties and the Department of Municipal Affairs. A questionnaire was suggested to be sent to all or selected municipalities.

At the next meeting held on May 17, 1985, the Consultants informed the Committee on the meetings with several individuals and on the pertinent comments made. The Committee was also advised on the borrowing practices of other provincial agencies. The Committee perused the 27 suggested points included in the questionnaire, eventually mailed to 83 selected municipalities.

At the meeting held on July 3, 1985, the Consultants briefed the Committee on the results of the returned and completed questionnaires and on the further meetings they held with the representatives of different municipalities, provincial departments and others.

At the meeting held on August 15, 1985, the Consultants submitted to the Committee five proposed guidelines and asked the members' reaction to same. They also highlighted the additional interviews held with mainly provincial representatives.

At the last meeting held with the Consultants on October 1, 1985, they submitted their Draft Report for discussion. Their recommendation was to use the following six criteria as guidelines with suggested numerical limits:

1. debt magnitude;
2. debt burden;
3. financing burden;
4. enterprises;
5. current tax burden;
6. projected tax burden.

While the Committee accepted the theory and justification of the proposed guidelines, they expressed concerns about the implementation and the complexity of the eleven worksheets and the seven trend schedules that would be required to be completed by municipalities applying for debenture borrowing. The Committee recommended that the Consultants arrive at a more workable and simplified version of the recommended guidelines.

Accordingly, the final revised Report and Executive Summary was submitted by the Consultants on October 15, 1985.

The Committee met, without the Consultants, for the last time on October 31, 1985, considered the Consultants' Report and arrived at the recommendations to the Minister of Municipal Affairs.

RECOMMENDATIONS

1. **THE COMMITTEE RECOMMENDS THAT THE LOCAL AUTHORITIES BOARD BE REQUIRED TO ESTABLISH THE FIVE GUIDELINES OUTLINED IN THE CONSULTANTS' REPORT.**

It became obvious from the extensive studies conducted by the Consultants that the establishment of borrowing guidelines is not only necessary but it is overdue.

It was also evident that no single formula, ratio or criterion would properly and accurately determine whether a given municipality exceeded the safe limits of its financial capacity.

The Consultants originally recommended the use of eleven guidelines and the completion of eleven worksheets for each borrowing application. The Committee would not concur. In the era of deregulation, it may be unwise to introduce the requirement for extensive calculations and work.

Accordingly, it is recommended that the guidelines and the guideline amounts to be established shall be limited to the following:

a) total debt magnitude
- (total debt as a percentage of Equalized Assessment)
- 30% for cities, towns, villages
- 15% for summer villages, counties, municipal districts

b) total debt burden
- (debt service charges as a percentage of revenue)
- 35% for cities, towns, villages
- 20% for summer villages, counties, municipal districts

c) total financing burden
- (normalized debt service costs as a percentage of revenue)
- 40% for cities, towns, villages
- 25% for summer villages, counties, municipal districts

d) tax burden - current
- 100 mills of Equalized Assessment for all municipalities

e) tax burden - projected
- (tax increase due to current year and proposed borrowing)
- annual rate of inflation for all municipalities.

These guidelines are determined by the use of Worksheets #1 to #4 of the Consultants' Report and copies are also attached.

The use of the additional six guidelines, amounts and the requirements to complete the other six worksheets to be left to the discretion of the Local Authorities Board for applications that fail to meet the basic five guidelines and amounts.

2. THE COMMITTEE RECOMMENDS THAT THE COMPLETION OF SCHEDULES A TO G OUTLINED IN THE CONSULTANTS' REPORT NOT BE REQUIRED AT THIS TIME.

As the completion of the seven forms would create additional work for the municipalities, the introduction of such requirements may be contradicting the intent of deregulation.

The Committee recommends that all the information related to trend analyses of debt charges, operations and capital, liquidity, taxes, assessment and demography be calculated by the Local Authorities Board and stored in their system and made available to individual municipalities at their request.

3. THE COMMITTEE RECOMMENDS THAT CITIES AND TOWNS BE REQUIRED TO PREPARE A FIVE YEAR LONG-TERM CAPITAL BUDGET AND SAME BE FILED WITH THE LOCAL AUTHORITIES BOARD ANNUALLY.

At the present, the majority of municipalities do not prepare a long-term capital budget and their borrowings are on an ad-hoc basis. The requirement of proper planning for at least five years ahead is considered a proper financial, business and educational procedure.

4. THE COMMITTEE RECOMMENDS THAT THE LOCAL AUTHORITIES BOARD ADVISES THE MUNICIPALITIES OF THE SAVINGS BY REPAYING DEBENTURES IN EQUAL ANNUAL PRINCIPAL PAYMENTS PLUS INTEREST FOR FUTURE BORROWINGS.

While school authorities repay their debentures in equal annual principal payments, plus interest, municipalities use equal annual blended payments of principal and interest. The savings in the former method are very considerable as interest costs are gradually reduced.

5. THE COMMITTEE RECOMMENDS THAT THE LOCAL AUTHORITIES BOARD CONDUCTS SEMINARS FOR MUNICIPAL PERSONNEL REQUIRED TO COMPLETE THE GUIDELINE WORKSHEETS.

The worksheets proposed by the Consultants require the use of figures set forth by the auditors in the yearly municipal financial statements. For easy clarification purposes, each line of the five recommended worksheets clearly indicates the corresponding financial statement reference numbers. Accordingly, there should not be any difficulty in preparing the five worksheets. However, some municipalities have less experienced staff and they may encounter problems or fail to understand the procedure. For these reasons, the Local Authorities Board staff shall invite the municipal personnel involved to partake in one session, explain to them the process and answer questions. Each event shall be limited to 15-20 persons in order to achieve optimal benefit.

6. THE COMMITTEE RECOMMENDS THAT THE PROVINCIAL GOVERNMENT RE-EVALUATE ALL THE GRANT PROGRAMS AVAILABLE TO MUNICIPALITIES.

During the interviews conducted by the Consultants, one of the most commonly held views was that the Province encouraged borrowing with several grant programs that fund a portion of the capital cost of certain projects. The Departments of Municipal Affairs, Culture, Economic Development, Environment, Recreation and Parks, Transportation, Utilities and Telecommunications and Alberta Mortgage and Housing Corporation offer grants affecting capital expenditures. There is a pressing need for correlation between the above-mentioned departments and agency in the planning and approval process of grants.

Guideline
Worksheet #1

_____
Name of Municipality

TOTAL DEBT MAGNITUDE

Part a) December 31, 19 ____

Total Debt:

	Total short-term loans and overdrafts	FS2-2-26	$_____
+	Debentures, bonds and mortgages	FR11-4-51	_____
+	Long-term borrowing and capital leases	FR12-4-51	_____
+	Long-term borrowing for operations	FR13-4-51	_____
+	AMHC debt (not included above)		_____
=	Total Debt		$_____ (A)

Equalized Assessment (most recent year - 19 ___) $_____ (B)

Total Debt as a % of Equalized Assessment A ÷ B _____%

Part b) Impact of Additional Borrowings

Change in Total Debt (AA) $_____

Adjusted Total Debt as a % of Equalized Assessment
(A + AA) ÷ B _____%

Guideline
Worksheet #2

_____
Name of Municipality

TOTAL DEBT BURDEN

Part a) December 31, 19 ____

Total Debt Service Charges:

	Short-term interest	FR19A-30	$_____
+	Long-term debt charges	FR19A-31	_____
+	Debenture debt charges	FR19A-32	_____
=	Total Debt Service Charges		$_____ (C)

Total Revenue:

	Total general municipal revenues	FS3-1-61	$_____
+	Special municipal levies	FR19A-1	_____
+	Sales to other governments	FR19A-2	_____
+	Sales of goods and services	FR19A-3	_____
+	Professional and other licences and permits	FR19A-4	_____
+	Municipal by-law fines issued	FR19A-5	_____
+	Return on investments	FR19A-6	_____
+	Rental revenues	FR19A-7	_____
+	Other revenues from own sources	FR19A-8	_____
+	Other	FR19A-17	_____
=	Total Revenue		$_____ (D)

Debt Service Charges as a % of Revenue C ÷ D _____%

Part b) Impact of Changes

Change in:

Total Debt Service Charges	(BB)	$_____
Total Revenue	(DD)	$_____

Adjusted Debt Service Charges as a % of Revenue
(C + BB) ÷ (D + DD) _____%

Guideline
Worksheet #3

_____
Name of Municipality

TOTAL FINANCING BURDEN

Part a) December 31, 19 ____

Normalized Annual Debt Service Costs:

	Short-term interest	FR19A-30	$_____
+	Long-term debt charges	FR19A-31	_____
+	Debenture debt charges	FR19A-32	_____
-	Reduction* in debentures, bonds and mortgages	FR11-3-51	_____
-	Reduction* in long-term capital borrowing and capital leases	FR12-3-51	_____
-	Reduction* in long-term borrowing for operations	FR13-3-51	_____
=	Total Annual Interest Costs		_____ (E)
+	5% of Total Debt	.05 x (A)	_____
=	Normalized Debt Service Costs		_____ (F)

Total Revenue (D) $_____

Normalized Debt Service Costs as a % of Revenue F ÷ D _____%

Part b) Impact of Changes

Change in:

Total Interest Costs (CC) $_____

Total Debt (AA) $_____

Total Revenue (DD) $_____

Adjusted Normalized Debt Service Costs as a % of Revenue (F + CC + .05 x AA) ÷ (D + DD) _____%

* Reductions should exclude any interfunction debt transfers included in the total reductions.

Guideline
Worksheet #4

_____
Name of Municipality

Part (a) TAX BURDEN - CURRENT (Equalized Mill Rate)

	Total taxes and grants in lieu	FS5-2-10	$_____
+	Net deficit for year	FS3-3-63	_____
	Total		$_____ (G)

Equalized Assessment (most recent) (B) $_____

Equalized Mill Rate (G ÷ B) x 1000 _____ (H)

Part (b) TAX BURDEN - PROJECTED
(New Borrowing Tax Burden - Net General Borrowing Only)

Annual debt service costs for proposed (net) general borrowing and (net) general borrowing approved since the last year end (JJ) $_____

Total taxes and grants in lieu (above) FS5-2-10 $_____ (I)

Total Increase JJ ÷ I _____%